What is the Difference Between Occurrence vs. Claims Made Forms?

All the property and casualty insurance policies you buy fall into one of two categories - "occurrence" or "claims-made." This distinction may impact drastically on:

1. Whether or not your policy will respond to a claim;
2. What your responsibilities will be in the event of a claim;
3. How much your policy will cost up front and in subsequent years, and;
4. How much it will cost to keep the coverage in effect, in the event of cancellation.

With all this riding on the type of coverage form you purchase; it helps to understand the pros and cons of each so that you can make an informed decision if options are available.

"Occurrence" form coverage is the simpler of the two. Most property and casualty insurance policies fall into this category. Quite simply, "occurrence" form coverage means that the policy responds to events that occur during the policy period regardless of when the claim is made. Once the policy period is over, the policy will respond to covered claims, even if the claim is made many years after the triggering event (accident, wrongful act, injury, etc.).

The far more complex "claims-made" coverage form responds only to claims that are made during the policy period, though the triggering event may occur prior to the policy period if there is a "retroactive date" on the policy. The key to "claims-made" policies is maintaining continuous coverage. Without "continuity," insurers will not give you that all important retroactive coverage.

"Claims-made" coverage came into vogue in the sixties and seventies as professional liability policies gained a foothold and underwriters sought to contain the volatile nature of the "tail." In property and casualty insurance lingo the "tail" refers both to the optional coverage that may be purchased to extend the policy for reporting purposes, and to the typical length of time between the triggering event and the claim. Asbestosis, which often takes years to develop, is considered a "long tail" exposure. Libel and slander lawsuits, on the other hand, usually occur right after the triggering event, i.e., libelous newspaper article or news broadcast.

"Claims-made" policies are becoming more popular in commercial lines because soon after the policy year is over, actuaries will have a pretty good idea of how many more claims might be reported. Subsequent claims, even if the triggering event occurred during that earlier policy period, will be charged to the later policy period when the claim is made. The ability to "close out" policy years quickly, is a palpable benefit to insurers of the "claims-made" form.

How do you identify "claims-made" or "occurrence" policies? "Claims-made" policies are easier to identify because they will typically advise you in the declarations or the first page of the policy: "THIS IS A CLAIMS-MADE POLICY." Additionally, you can search for Extended Reporting Period, aka "tail" option, provisions in the form. A space for "retroactive date" on the declarations page is another telltale sign of "claims-made."

"Occurrence" policies are more difficult to spot. While some policies might herald the occurrence nature of the form, in other cases it will be the lack of "claims-made" language and provisions that will provide the clues.

While "claims-made" might seem more onerous than "occurrence," for the buyer there are some benefits that warrant mentioning. First and foremost, there is the pricing issue. The first year of "claims-made" coverage should typically cost somewhere between 40 and 85% of an "occurrence" policy. The price automatically increases in subsequent years as the "claims-made" exposure increases. Usually, after three to five years, a
"claims-made" policy is thought to be roughly equivalent to an "occurrence" policy and should cost about the same. In addition to the cost savings enjoyed early in the early years of coverage, in a competitive marketplace insureds can benefit as underwriters discount the step factors that bring up the price. Also, although Extended Reporting Period options can be quite costly, it is rare that an insured will need to exercise such an option unless they retire or are unable to find retroactive coverage from another carrier. Still, it's a good idea to compare Extended Reporting Period options if you are presented with quotes from different carriers. How long are the "tail" options and how expensive?

While "claims-made" coverage can be confusing, it's clear this coverage form is here to stay as the preferred choice for insurers across an increasingly broad array of product lines. So get used to the concept now and be prepared to explore all the options carefully.